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In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 287

ALDUS C. HIGGINS, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 71–81) is reported in 44 B. T. A. 1123. The opinion of the United States Circuit Court of Appeals (R. 89–100) is not yet reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 2, 1942 (R. 100). The petition for a writ of certiorari was filed on August 7, 1942. The jurisdiction of this Court is invoked

under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether transfers in trust in 1920 which reserved power in the grantor to alter the distribution of the income and corpus as between designated beneficiaries, but not to revest any of the beneficial interest in himself, are subject to the gift tax in 1938 when the grantor surrendered his reserved power.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra,* pp. 11–14.

STATEMENT

The facts as stipulated (R. 33–65) and as found by the Board of Tax Appeals (R. 71–77) may be summarized as follows:

Aldus C. Higgins, the taxpayer, created two trusts in 1920, one for the benefit of his daughter Elizabeth and her issue (R. 38), the other for the benefit of his son Milton and his issue (R. 50). Since there is no material variation between the two trusts, it is sufficient to state the facts pertinent to the trust for Elizabeth. The taxpayer declared himself the trustee of 662 shares of the capital stock of the Norton Company for the benefit of Elizabeth, her children, and the issue of any such child or children. The trust was to

continue until her death and thereafter until each of her children should have reached the age of 21 years or died. At the termination of the trust the principal was to be distributed pro rata among her then surviving children and the then surviving issue of any deceased child or children by right of representation. There was, however, the possibility of an earlier final distribution of the whole or any part of the trust fund pursuant to certain powers enumerated in the trust instrument. (R. 38–44.)

Taxpayer reserved to himself as settlor "full power and authority to appoint to any beneficiary the whole or any part of the principal of the trust fund." This power could be exercised by will or by deed *inter vivos* and might be so employed as to effectuate immediate "payment and delivery of that portion of the trust fund" so appointed (R. 42). The settlor also reserved to himself power by will or by deed "to modify the terms of this instrument either as to the powers of the trustees with respect to investments or as to their powers with respect to the distribution of income or principal among the beneficiaries herein named or described prior to the termination of the trust" (R. 43). Also, the settlor reserved power to appoint additional trustees, to remove any trustee or trustees, to fill vacancies among the trustees, "or he may refrain from appointing

trustees to such places, and the number of trustees shall be augmented or reduced accordingly" (R. 39).

In his capacity as trustee the taxpayer was given by the trust instrument sweeping powers of management of the trust funds. The trustees were empowered either (a) to accumulate the income, (b) to "apply the same in any way for the support, comfort and education, either in my own household or elsewhere, or otherwise to the benefit of the beneficiaries or any of them," or (c) to "pay over the same either in money or otherwise to the beneficiaries or any of them" (R. 41). The trustees were also given full power and authority to apply to the care, support, education, or otherwise to the benefit of any beneficiary, so much of the principal as they should deem necessary to the health, comfort, education, or otherwise to the best interests of any such beneficiary (R. 41–42).

On March 10, 1938, the taxpayer resigned as trustee and appointed Katharine H. Riley to act as trustee in his stead (R. 34–35, 48–49). On the same day, by virtue of his reserved powers, taxpayer executed a formal instrument amending the provisions of the trust so as to broaden somewhat the discretionary powers of the trustees with reference to the disposition of income and principal; and by the same instrument he released and relinquished "all powers reserved or given to me

by any and all of the provisions of said trust instrument" (R. 35, 48–49).

The Commissioner ruled that the relinquishment of these powers constituted gifts of the whole corpus of each trust fund (R. 7–16). The Board of Tax Appeals sustained the Commissioner and determined a deficiency in gift tax for the year 1938 in the sum of $283,362.65 (R. 85). On appeal by the taxpayer the court below affirmed the decision of the Board (R. 100).

ARGUMENT

1. The case is controlled by the decisions of this Court in *Estate of Sanford* v. *Commissioner,* 308 U. S. 39, and *Rasquin* v. *Humphreys,* 308 U. S. 54, which were followed by the court below (R. 97, 99–100). Those decisions establish that a gift in trust is incomplete if power is reserved in the donor to change the beneficiaries or otherwise alter the disposition of the property, although not to the donor's benefit, and that only upon relinquishment of the power does the transfer become subject to the gift tax. Accordingly, not until 1938 when petitioner resigned as trustee and surrendered his reserved powers did the gifts here involved become taxable.

(a) Petitioner asserts (Pet. 9–10) that the control over the economic benefits of the property here involved passed when the trusts were created, whereas the opposite was true in the *Sanford* case.

But this claim is without substance. The only factual difference relied on to support the claim is that petitioner, unlike the taxpayer in the *Sanford* case, could not substitute new beneficiaries, but could only alter the distribution as between those already designated.

If a transfer is incomplete where the donor reserves the power to alter the benefits receivable by persons other than himself, as was held in the *Sanford* and *Humphreys* cases, there is no sound reason why one should be considered any less incomplete where he reserves the power to change the benefits to be received by members of a limited class of such persons. In neither instance has he made a final transfer to a particular donee or given up the control of the economic benefits in a comparable sense. Thus, the courts have held repeatedly that the corpus of a trust is subject to the estate tax where the grantor has reserved the power to eliminate one or more beneficiaries or to vary the shares distributable to them. *Chickering v. Commissioner,* 118 F. (2d) 254 (C. C. A. 1), certiorari denied, 314 U. S. 636; *Cook* v. *Commissioner,* 66 F. (2d) 995 (C. C. A. 3), certiorari denied, 291 U. S. 660; *Guggenheim* v. *Helvering,* 117 F. (2d) 469 (C. C. A. 2), certiorari denied, 314 U. S. 621; *Holderness* v. *Commissioner,* 86 F. (2d) 137 (C. C. A. 4); *Millard* v. *Maloney,* 121 F. (2d) 257 (C. C. A. 3), certiorari denied, 314 U. S. 636; *Commissioner* v. *Chase Nat.*

Bank, 82 F. (2d) 157 (C. C. A. 2), certiorari denied, 299 U. S. 552.

(b) Petitioner contends (Pet. 5, 13–14) that if the transfers in the present case were incomplete for gift tax purposes prior to 1938, they remained the same thereafter because, concurrently with surrendering his reserved powers, petitioner vested similar powers in the trustees. The court below answered this contention by pointing out that the gift tax is imposed upon the transfer by the donor, rather than upon the receipt by the donees, and that petitioner's action in 1938 made the case the equivalent of one in which a donor transfers property in trust for named beneficiaries without reserving any power in himself but vesting power in the trustees to allocate income or principal among the beneficiaries (R. 98). In such a case it would hardly be claimed that the transfer would not be subject to the gift tax; and any such contention would be rejected.

Cockrell v. *United States,* 39 F. Supp. 148 (C. Cls.), is not in conflict with this conclusion, but is in accord with the decision of the court below. The grantor in that case reserved the power to confer additional powers upon the trustees, including the power to change the beneficiaries or, upon certain contingencies, to revest the corpus in the grantor, and under the *Sanford* decision this reservation of power in the grantor was held sufficient to render the gift incomplete. In the in-

stant case the grantor forfeited all his reserved powers in 1938 and thereby gave up all control of the economic benefits.

2. The court below did not err in refusing to apply Article 3 of Treasury Regulations 79 as promulgated in 1936 (Appendix, *infra,* pp. 13–14). Those regulations, until amended in 1940 to conform with the decisions in the *Sanford* and *Humphreys* cases (Appendix, *infra,* pp. 12–13), provided that a transfer is complete for purposes of the gift tax unless the donor reserves the power to cause the beneficial title to be revested in himself. However, this Court held in the *Humphreys* case that whatever validity the regulations might have as applied prospectively, they were so plainly in conflict with the statute as to preclude them from being applied retroactively to the transfer made by the creation in 1934 of the trust there involved (308 U. S. 54, 56). Similarly, they may not be applied to the transfers effected in 1920 by the creation of the trusts in the present case. It follows under this Court's decisions in both the *Sanford* and *Humphreys* cases that the transfers became taxable in 1938 and that, as was held by the court below (R. 100), this result would be required without regard to the 1940 amendments to the regulations. Accordingly, apart from other distinctions, there is no conflict with *Helvering* v. *R. J. Reynolds Tobacco Co.,* 306 U. S. 110, where retroactive effect was denied an amended regula-

tion which changed valid preexisting regulations of long standing.

3. Since the holding of the court below is in harmony with the decisions of this Court in the *Sanford* and *Humphreys* cases and does not conflict with the holding of any lower court rendered subsequent to those decisions, there is no occasion to consider the validity of the views expressed in the opinion of the court below regarding proper correlation of the gift with the estate and income taxes. Neither the different views of petitioner nor the decisions cited in the petition illustrating the absence of correlation between gift and estate taxes in certain other situations furnishes any basis for certiorari.[1] This Court has indicated that the principal problem is to correlate the estate and gift taxes, but has recognized, as did the court below (R. 92–96), that even that desirable end is not possible of perfect accomplishment under the existing statutes. *Estate of Sanford* v. *Commissioner, supra,* pp. 43–46.

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[1] The decisions cited on pages 3–4 of the petition as being in conflict with the decision of the court below present instances in which both a gift tax and an estate tax may be imposed. In none, however, was it held that a transfer was subject to gift tax where the grantor reserved in himself the power to alter the distribution of the property. *Commissioner* v. *Prouty*, 115 F. (2d) 331 (C. C. A. 1); *Helvering* v. *Robinette* (C. C. A. 3), decided March 23, 1942; *Helvering* v. *Marshall*, 125 F. (2d) 943 (C. C. A. 2); *Chase National Bank* v. *United States*, 116 F. (2d) 625 (C. C. A. 2); *Lilly* v. *Smith*, 96 F. (2d) 341 (C. C. A. 7); *Commissioner* v. *McLean*, 127 F. (2d) 942 (C. C. A. 5).

CONCLUSION

The decision of the court below is correct and there is no conflict of decisions. The petition for certiorari should be denied.

Respectfully submitted.

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AUGUST 1942.